

SENATE BILL REPORT

SB 5011

As of March 9, 2017

Title: An act relating to the business corporation act.

Brief Description: Concerning the business corporation act.

Sponsors: Senators Pedersen, Padden, Frockt, Fain and Kuderer; by request of Washington State Bar Association.

Brief History:

Committee Activity: Law & Justice: 1/10/17.

Brief Summary of Bill

- Establishes a statutory procedure for ratifying and validating defective corporate actions.
- Authorizes forum selection provisions for internal corporate disputes.
- Permits asset drop-down transactions without approval by parent corporation's shareholders.
- Eliminates ten-year term limits on voting trusts and voting agreements.
- Permits short-form downstream mergers.

SENATE COMMITTEE ON LAW & JUSTICE

Staff: Melissa Burke-Cain (786-7755)

Background: Delaware is considered a leading state for corporate jurisprudence because of its long history as an incorporation-friendly state. In 2013, the Delaware court ruled that errors in authorizing corporate action could not be retroactively corrected. The American Bar Association (ABA) updated its model corporations law to allow a corporation to retroactively validate or ratify authorization errors. Delaware also changed its laws to authorize retroactive correction of faulty authorizations of corporate action. Recently, shareholder lawsuits challenging internal corporate operations have increased and are sometimes filed in multiple locations at the same time, causing excessive legal costs. Delaware amended its

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

business corporations laws to permit corporate governing documents to designate the forum for lawsuits.

Current Washington business corporations law is not consistent with the ABA model law or with Delaware law regarding approval of drop-down transactions. A drop-down transaction is an asset transfer from a parent company to its wholly owned subsidiary. Both the ABA model law and Delaware's law permit a board of directors to approve a drop-down asset transfer without shareholder approval. The parent corporation's shareholders must approve any subsequent asset transfers by the subsidiary. Current Washington business corporation laws permit shareholders to arrange for voting their shares using a voting trust, a shareholders' agreement, or a voting agreement, although voting trusts have a ten-year duration and shareholders' agreements are presumed to end after ten years. The updated approach used by the ABA model law and Delaware law have no express or presumed end date for shareholder voting arrangements. A short-form merger allows a parent corporation and related subsidiary to merge without shareholder approval when the parent corporation owns 90 percent of the shares of the subsidiary. Washington's business corporations law allows a short-form merger without a shareholder vote when the subsidiary merges into the parent company but not if the parent company merges into the subsidiary. In this respect, Washington's law is inconsistent with the ABA model law, and those of 33 other states, including California, Delaware, and New York.

Summary of Bill: A business corporation may designate the forum court for filing internal disputes in its governing documents. A business corporation may transfer assets to a wholly-owned subsidiary corporation without a shareholder vote approving the transfer. If the wholly-owned subsidiary makes a subsequent asset transfer, the parent corporation's shareholders must approve the subsidiary's asset transfer. A business corporation may correct a defect in an authorization of corporate action by a validating vote of the board of directors or by a ratifying vote of the shareholders when the defective authorization is discovered. The correction validates the action back to its original date. A parent corporation and a subsidiary may merge using a short-form merger, without shareholder approval, if the parent company owns 90 percent of the stock of the subsidiary. The corporation may use the short-form merger if the parent company merges into the subsidiary or the subsidiary merges into the parent company. A shareholder voting trust is not limited to a ten-year maximum duration. A shareholder voting agreement is not presumed to have a ten-year maximum duration.

Appropriation: None.

Fiscal Note: Not requested.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: The WSBA's committee that reviews our corporations law regularly proposes updates to Washington's laws so that our state remains a viable incorporation choice when compared with Delaware and other corporation-friendly states. The bill clarifies the business corporations law and responds to evolving corporations jurisprudence in other jurisdictions in five main areas. The bill creates a statutory process for

correcting a mistake when authorizing corporate action. It safeguards the correction process from misuse by requiring evidence that the corporation tried to take action and by providing sixty days to seek judicial review of the correction process. Corporations may select a court forum for internal corporate disputes to avoid defending the same lawsuit in multiple courts at the same time. The bill eliminates the ten-year reauthorization requirement for voting trusts and the ten-year duration for voting agreements from an outdated version of a model law. Asset drop down transactions will now require shareholder approval of asset transfers by a corporation's wholly owned subsidiary instead of the current requirement for shareholder approval, only when a corporation transfers assets to a subsidiary. The bill also authorizes short form mergers up and downstream between operating corporations and holding companies.

Persons Testifying: PRO: Senator Pedersen, Prime Sponsor; Michael Hutchings, WSBA.

Persons Signed In To Testify But Not Testifying: No one.